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OLN - Q3 2013 Olin Earnings Conference Call

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OVERVIEW:

OLN reported 3Q13 sales of \$670.7m and net income of \$69.7m and \$0.86 per diluted share. Expects 4Q13 diluted EPS to be \$0.25-0.30.



CORPORATE PARTICIPANTS

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PRESENTATION

Operator

Good Day and welcome to Olin's third quarter 2013 earnings conference call. All participants will be in listen only mode.

(Operator Instructions)

After today's presentation, there will be an opportunity to ask questions.

(Operator Instructions)

Please note this event is being recorded. I would now like to turn the conference over to Mr. Joseph Rupp, Chairman, President and CEO. Mr. Rupp, the floor is yours, sir.

Joseph Rupp - Olin Corp - Chairman, President and CEO

Thank you. Good morning and thank you for joining us today. With me this morning are John Fischer, Senior Vice President and Chief Financial Officer; John McIntosh, Senior Vice President of Operations; and Larry Kromidas, our Assistant Treasurer and Director of Investor Relations.

Last night, we announced that net income in the third quarter of 2013 was \$69.7 million or \$0.86 per diluted share, which compares to \$28.7 million or \$0.35 per diluted share in the third quarter of 2012. Sales in the third quarter of 2013 were \$670.7 million, compared to \$581.2 million in the third quarter of 2012. Olin had a strong third quarter of 2013, during which we increased our cash position by \$142.2 million. We also generated \$138.8 million of adjusted EBITDA, which is the highest quarterly level in the history of the Company. The record adjusted EBITDA was driven by strong volumes and reduced costs in the Winchester business. The elevated level of commercial demand that Winchester began to experience in the fourth quarter of 2012, continued throughout the third quarter of 2013.



Third quarter 2013 commercial sales increased approximately 29%, compared to the third quarter of 2012, and as a result, Winchester achieved the highest level of quarterly earnings in its history. Third quarter Olin 2013 earnings included \$1.6 million of pretax restructuring charges, the net recovery of \$11.4 million of pretax legacy legal costs, and then \$8.8 million of favorable tax adjustments. In the third quarter of 2013, Chlor Alkali segment earnings improved compared to the third quarter of 2012 levels due to a favorable contract settlement, which more than offset weaker shipments of chlorine and caustic soda. Early in September, the business began to experience a slowdown in chlorine demand, which continued through the balance of the quarter. As a result, year-over-year third quarter 2013 chlorine and caustic soda shipments declined by 2%.

Fourth quarter 2013 net income was forecast to be in the \$0.25 to \$0.30 per diluted share range, which is expected to include a pretax gain of approximately \$5 million from the sale of a joint venture interest and approximately \$5 million of favorable tax adjustments. Fourth quarter 2013 earnings are also forecast to include approximately \$2 million of pretax restructuring charges, and \$4 to \$5 million of legacy environmental expense, compared to \$700,000 in the third quarter of 2013. Chlor Alkali volumes and netbacks are forecast to decline compared to both the fourth quarter of 2012 and the third quarter of 2013. Fourth quarter 2013 Chlor Alkali and Chemical Distribution earnings will also reflect normal seasonal weakness in bleach sales. Fourth quarter 2013 bleach sales are forecast to decline from third quarter 2013 levels approximately 25%. Winchester earnings are forecasted to decline from third quarter 2013 levels, due to normal seasonal weakness in hunting sensitive products, but they will improve when compared to the fourth quarter of 2012.

In spite of a relatively weak operating environment in both the Chlor Alkali and Chemical Distribution businesses, we had a strong third quarter of 2013. The quarterly adjusted EBITDA was the highest quarterly level in the history and we are on track to generate a record level of full year adjusted EBITDA.

Third quarter 2013 chlorine and caustic soda shipments declined by approximately 2%, compared to the third quarter of 2012, and also declined approximately 1% compared to second quarter 2013 levels. Olin's third quarter 2013 operating rate was 86%, but it declined sequentially as we moved through the quarter and was 79% in the month of September. The third quarter 2012 operating rate after giving consideration to the 2012 capacity reduction of 160,000 tons was also 86%.

During the third quarter of 2013, chlorine shipments to urethane customers declined approximately 50%, while shipments to titanium dioxide customers increased approximately 4%. In the Olin system, the quarter to quarter trend in shipments of chlorine to urethane customers has remained volatile, and we have seen a longer term downward trend in chlorine shipments to titanium dioxide customers. During the third quarter, the weaker level of chlorine shipments were offset by a higher level of bleach shipments. Third quarter 2013 bleach shipments reached the highest quarterly level ever and increased 14% compared to the third quarter of 2012. This represents the 23rd consecutive quarterly year-over-year increases in bleach shipments. The third quarter 2013 bleach shipments totaled approximately 57,000 ECUs, and the combination of hydrochloric acid and bleach shipments in the third quarter of 2013 represented approximately 20% of the available capacity in the Olin system. During the fourth quarter of 2013, we expect bleach volumes to decline, compared to third quarter, which reflects a normal seasonal slowdown as we exit bleach season.

Over the past five years, fourth quarter bleach shipments have declined between 20% and 30%, when compared to third quarter levels. As the bleach component of the Chlor Alkali business continues to grow, the seasonal impact on both the Chlor Alkali operating rate and segment earnings will increase, and this is a factor impacting the fourth quarter 2013 earnings outlook. As a point of reference, since 2006, Olin's fourth quarter operating rate has on average been 10 percentage points lower than the third quarter rate.

Hydrochloric acid shipments in the third quarter of 2013 were similar to the third quarter of 2012, but the year-over-year price declined approximately 30%. This reduced the third quarter profit contribution from this product by approximately \$4 million, compared to third quarter 2012 levels. On a year-to-year basis, the 2013 profit contribution from hydrochloric acid has declined approximately \$14 million, compared to the first nine months of 2012. The decline reflects the product shortages that occurred in 2012 that resulted in unusually strong pricing. That said, we continue to view hydrochloric acid as an important value added product for Olin, and during 2013, hydrochloric acid has commanded a price premium compared to chlorine of approximately \$150 per ton. As we move forward, we expect hydrochloric acid shipments to grow.

Freight costs per ECU in the third quarter of 2013 increased approximately 4%, compared to the third quarter of 2012. On a year-to-date basis, freight costs per ECU in 2013 have increased less than 3%, compared to the 2012 levels. During the third quarter, the ECU netback was approximately \$570 per ton, compared to approximately \$560 per ton in the third quarter of 2012, but down from the second quarter of 2013 level of approximately



\$575 per ton. This sequential decline in ECU netbacks did not meet our expectations of a sequential improvement, and reflects caustic soda pricing that was essentially flat in our system, and slightly lower chlorine pricing. During the third quarter, the caustic soda price indices, declined \$50 per ton, and this will negatively impact Olin's fourth quarter ECU netbacks.

Consistent with prior years, we expect Chlor Alkali operating rate to decline from the 86% third quarter 2013 rate, to a fourth quarter rate in the mid-70s. Based on this level of caustic soda demand, we are currently experiencing, at the mid-70% range in the fourth quarter, this will result in a shortage of caustic soda. For this reason, we believe that the decline in the caustic soda price indices should not be sustained. Over the past year, the published export price for caustic soda has declined relative to the domestic price. Olin's Chlor Alkali production is diversified geographically, which allows us to concentrate our caustic soda sales domestically and export minimal quantities. The third quarter 2013 Chlor Alkali segment income was \$64.4 million, which included an \$11 million favorable contract settlement. Pricing across all the products was similar to the third quarter of 2012, with the benefits of higher caustic soda prices offset by lower chlorine and hydrochloric acid prices.

Both electricity costs and outage-related maintenance causes were higher in the third quarter of 2013, compared to the third quarter of 2012. The third quarter Chlor Alkali segment earnings equate to quarterly EBITDA of \$90.1 million. Fourth quarter 2013 Chlor Alkali segment earnings are forecast to decline compared to both the third quarter of 2013 and the fourth quarter of 2012. The year-over-year fourth quarter decline reflects lower ECU netbacks and the absence of the \$9 million of one-time gains that were included in the fourth quarter 2012 results.

Now turning to Chemical Distribution, during the third quarter of 2013, the Chemical Distribution segment earned \$3.4 million, compared to \$1.9 million in the third quarter of 2012. The third quarter of 2012 reflects 39 days of ownership by Olin. The third quarter 2013 earnings represent \$7.2 million of quarterly segment EBITDA. In the third quarter of 2013, the business experienced a decline in caustic soda sales of approximately 12%, compared to the second quarter of 2013, but saw gross margins per ton improve 26%, compared to the second quarter. This improvement reflects the combination of slightly higher selling prices and lower caustic soda acquisition costs.

Third quarter 2013 bleach volumes increased approximately 9%, compared to the second quarter level of 2013. The third quarter is typically the strongest quarter of the year for Chemical Distribution bleach sales, and bleach sales represented approximately 10% of the total third quarter 2013 Chemical Distribution sales and a greater percentage of the profit contribution. Third quarter 2013 Chemical Distribution sales also included quantities of Olin produced hydrochloric acid, and potassium hydroxide, products not sold by the business prior to the acquisition. We expect Chemical Distribution sales and earnings in the fourth quarter of 2013 to decline, compared to the third quarter of 2013 due to normal seasonal weakness in the sales of both caustic soda and bleach.

In 2013, we have been disappointed by the financial performance of the business. During the second quarter, we discussed the negative impact that rising caustic soda prices typically have on a distributor. We've also experienced aggressive pricing in the caustic soda market, from large global distributors, and have observed some realignment of the caustic producer, caustic distributor relationships. That said, we continue to believe in the business, and are aggressively pursuing profit improvement initiatives. Significant synergies will be realized from selling Olin produced products, such as hydrochloric acid, bleach, and potassium hydroxide, as well as the continued integration of the Chemical Distribution and Chlor Alkali transportation and logistics capabilities. The capability to handle and sell these Olin produced products has progressed, and we remain positive on the outlook for the business.

And now Winchester. During the third quarter of 2013, commercial demand continued at the surge levels that began in the fourth quarter of 2012, resulting in a situation under which any product Winchester could produce, it was able to sell. As a result, the third quarter 2013 commercial sales increased 29%, compared to third quarter of 2012. In addition, third quarter 2013 law enforcement and military sales increased 17%, compared to third quarter of 2012. Third quarter 2013 Winchester sales of \$213.1 million increased approximately 8% compared to the second quarter of 2013 and were the highest level of quarterly sales in the history of the Company. While we expect fourth quarter 2013 sales to decline, compared to third quarter of 2013, due to the normal seasonal decline in hunting sensitive products, and due to two plant outages. We currently expect the high level of ammunition demand to continue into 2014.

The September 30, 2013 commercial backlog was \$439 million, and the total September 30, 2013 backlog was \$578 million. These compared to commercial backlog at September 30, 2012, of \$92 million, and total backlog of \$214 million. The combined effect of the record level of quarterly sales, improved product pricing, and lower manufacturing costs driven by the cost benefits associated with the centerfire ammunition relocation



to Oxford, Mississippi, resulted in Winchester generating a record level of quarterly segment income. Third quarter 2013 segment income was \$40.7 million, and the third quarter of segment EBITDA was \$44.4 million. During the third quarter of 2013, the cost savings realized from the ongoing centerfire relocation project were approximately \$3.5 million, and that compares to \$500,000 in the third quarter of 2012.

In the first 9 months of 2013, the relocation project has resulted in year-over-year profit improvement of approximately \$17 million. We now believe that the full year 2013 cost savings from the relocation will be approximately \$16 million, which represents a \$21 million year-over-year improvement, when compared to 2012. During 2013, the relocation of pistol ammunition manufacturing was completed, and the relocation of the rifle manufacturing was initiated. We continue to expect the entire relocation program to be completed by late 2015, or early 2016. Based on the cost savings that we have, that have been achieved to date, and the progress that has been made on overall relocation, we have increased the estimated annual cost savings that can be achieved at the completion of the relocation from \$30 million, to a range of \$35 to \$40 million.

Commodity metal costs on a per pound basis in the third quarter of 2013 were slightly higher than third quarter of 2012 levels, which created a year-over-year unfavorable variance of approximately \$1 million. On a year-to-date basis, 2013 commodity metal costs per pound have created a favorable variance of approximately \$3 million, when compared to 2012. The third quarter of 2013 unfavorable commodity cost variance compared to third quarter of 2012 was due to lead prices, which we expect to continue to generate unfavorable year-over-year comparisons in the fourth quarter of 2013, and the first half of 2014.

As we look ahead, we believe that Winchester's fourth quarter 2013 earnings will be lower than the third quarter 2013 level, but will improve compared to the fourth quarter of 2012. Looking beyond 2013, we expect commercial ammunition demand to continue at levels higher than the historic norm for the foreseeable future. This expectation reflects a significant increase in both gun ownership that has occurred over the past five years, as well as an increase in the number of people who have become regular target shooters. Based on survey data, we believe that over the past five years as many as 8 million new target shooters and therefore, ammunition consumers have been created. This is clearly a positive long-term trend for the commercial ammunition demand. The combination of the improved demand profile and the increase in the projected cost savings from the centerfire relocation project makes us believe the Winchester business can generate annual EBITDAs in the \$100 to \$110 million range.

I believe the cash flow performance of Olin in the third quarter of 2013, demonstrates the long-term potential that Olin has. Over the past three years, the investments we have made in acquiring the balance of SunBelt, the KA Steel distribution business, and relocating the Winchester centerfire ammunition operations to reduce costs and expanding our capacity to manufacture both bleach and hydrochloric acid have made the company less dependent on cyclical chlorine and caustic soda economics, while increasing the overall ability to generate cash.

The 2013 levels of cash flow should be further enhanced as we continue to increase the sales of bleach and hydrochloric acid, as well as make improvements to the Chemical Distribution business and realize synergies. Capital spending over the next several years should be in the \$85 million to \$100 million per year range. We continue to look for ways to deploy the cash and ways to increase shareholder value, and will continue to consider accretive acquisitions and investments, share repurchases, and our dividend policy. During the third quarter, we repurchased approximately 590,000 shares of stock, and we intend to be a consistent, steady, and opportunistic buyer of our shares over time.

Now I'd like to turn the call over to our Chief Financial Officer, John Fischer. John?

John Fischer - *Olin Corp - SVP and CFO*

Thanks, Joe.

First I would like to discuss the balance sheet and the third quarter 2013 cash flow. Cash and cash equivalents at September 30, 2013, including the restricted cash associated with the Go Zone financing that are classified as long-term assets on the balance sheet total \$290.4 million, compared to \$148.2 million at June 30, 2013.

During the third quarter of 2013, working capital employed declined by \$48 million from the second quarter 2013 levels. The largest component of this decline occurred in the Winchester business, due to declines in both receivables as normal seasonal dating payments were made and in inventories. Because of the high level of demand, Winchester was unable to affect a normal first half of the year inventory build and experienced



a quarter-to-quarter decline in the third quarter of approximately \$15 million. The Winchester September 30, 2013 inventory balance is approximately \$35 million lower than the September 30, 2012 level, and this decline is only been partially offset by higher receivables. The Chlor Alkali business, due to weakness in the second half of the third quarter, was able to reduce working capital during the quarter. Capital spending in the third quarter of 2013 was \$15.8 million, which is the lowest quarterly level since 2009, and approximately \$50 million lower than the third quarter 2012 level.

Depreciation and amortization expense in the third quarter of 2013 was \$34.1 million. We are now forecasting that full year 2013 capital spending will be approximately \$100 million, and we continue to forecast that full year 2013 depreciation and amortization expense will be in the \$135 million to \$140 million range. In 2014, we forecast that capital spending will be in the \$95 to \$105 million range, and that depreciation and amortization expense will remain in the \$135 to \$140 million range.

During the third quarter of 2013, we entered into a sale and leaseback transaction for the rail cars that were owned by the SunBelt joint venture. This was an opportunistic transaction, which allowed us to lock in long-term financing at a rate of approximately 3%, while utilizing expiring tax loss carryforwards to maximize the cash flow. The transaction generated \$35 million of cash during the third quarter. We currently expect that the September 30, 2013 cash balance will be maintained or grow slightly during the fourth quarter. During the fourth quarter, we will repay approximately \$12 million of maturing debt.

Now turning to the income statement. Selling and administration expenses decreased \$5.9 million, or 14% in the third quarter 2013, compared to the third quarter of 2012. This decline was due to the recovery of \$13.9 million of legacy legal costs in the third quarter 2013. During the third quarter 2013, there were also approximately \$2.5 million of legal expenses directly associated with this recovery. The benefit of this recovery was partially offset by expenses associated with the acquired Chemical Distribution operations of \$1.7 million, increased salary and benefit costs of \$1.4 million, and higher consulting fees of \$1 million. Selling and administration expenses as a percentage of sales were 5% in the third quarter, 2013, compared to 7% in the third quarter 2012.

Third quarter 2013 charges to income for environmental, investigatory, and remedial activities were \$700,000, compared to \$3.6 million in the third quarter of 2012. The third quarter of 2013 expense included a \$1.3 million recovery of environmental, investigatory and remedial activity costs incurred and expensed in prior periods. These charges relate primarily to expected future environmental investigatory and remedial activity associated with past manufacturing operations and former waste disposal sites. Fourth quarter 2013 expenses for environmental, investigatory and remedial activities are forecast to be in the \$4 to \$5 million range. We are not forecasting any recovery of environmental, investigatory and remedial costs incurred and expensed in prior periods in the fourth quarter 2013.

On a total company basis, defined benefit pension plan income was \$5.2 million in the third quarter of 2013, compared to \$5.6 million in the third quarter of 2012. We are not required to make any cash contributions to domestic defined benefit pension plans in 2013. In addition, under the pension funding relief provisions of the Moving Ahead for Progress in the 21st Century legislation that was enacted in 2012, we may not be required to make any additional cash contributions to our domestic defined pension plan for several years. During 2013, we do expect to make cash contributions to our Canadian defined pension plan of approximately \$1 million.

During the third quarter of 2013, Olin recorded a pretax restructuring charge of \$1.6 million, associated with the exiting of the use of mercury cell technology in the chlor alkali manufacturing process and the ongoing relocation of the Winchester centerfire ammunition manufacturing operations from East Alton, Illinois to Oxford, Mississippi. We currently expect that approximately \$6 million of additional pretax restructuring charges will be recorded over the next three years, associated with these activities.

The effective tax rate in the third quarter of 2013 was 25%, which included \$8.8 million of favorable tax adjustments primarily associated with the expiration of the statute of limitations on prior period returns. Excluding these adjustments, the effective tax rate was approximately 35%. For the full year 2013, we believe the cash tax rate which will reflect the benefits of accelerated depreciation, included in the 2010 Jobs Creation Act will be in the 15 to 20% range.

During the third quarter of 2013, approximately 590,000 shares of Olin stock were repurchased at a cost of approximately \$14 million under the July 2011, five-million share repurchase authorization. A total of 1.2 million shares have been purchased during 2013 at a cost of approximately



\$29 million. There are approximately 3.4 million shares remaining under the current authorization, and as Joe said earlier, we intend to continue to repurchase shares on a steady and opportunistic basis.

The third quarter results demonstrated the cash generation capabilities of the business, and we believe the company is well-positioned to continue to generate cash. As we move into 2014, capital spending will remain well below the level of depreciation and between now and 2016, we face less than \$40 million of required debt repayments and do not face any cash contributions to the large defined benefit pension plan. On October 24, Olin's Board of Directors declared a dividend of \$0.20 on each share of Olin common stock. The dividend is payable on December 10, 2013 to shareholders of record at the close of business on November 12, 2013. This is the 348th consecutive quarterly dividend to be paid by the Company.

Before we conclude, let me remind you that throughout this presentation, we have made statements regarding our estimates of future performance. Clearly, these are forward-looking statements, and results could differ materially from those projected. Some of the factors that could cause actual results to differ are described without limitations in the "Risk Factors" section of our most recent Form 10-K, and in our third quarter earnings release. A copy of today's transcript will be available on our website in the Investor Section under Calendar of Events. The earnings press release and other financial data and information are also available under Press Releases.

Operator, we are now ready to take questions.

QUESTIONS AND ANSWERS

Operator

Thank you, sir. We will now begin the question and answer section.

(Operator Instructions)

The first question we have comes from Frank Mitsch of Wells Fargo. Please go ahead.

Frank Mitsch - Wells Fargo Securities, LLC - Analyst

Good morning, gentlemen, and sorry about the Cardinals, but it's not over yet. (laughter).

Joseph Rupp - Olin Corp - Chairman, President and CEO

Thank you. It was excruciating.

Frank Mitsch - Wells Fargo Securities, LLC - Analyst

Yes, I can only imagine. Hey, this is a question on Chlor Alkali. Operating rates, similar year-over-year, I think you mentioned that as the quarter progressed, they have been coming down on the Chlor Alkali side. What do you attribute that to? And what are your expectations on an early read as to where we might see operating rates? I know you said down 10% is what you typically see in Q4, but what's your early read on expectations in 2014?

John McIntosh - Olin Corp - SVP, Operations

This is John, Frank.

We look at not only our own, but the industry operating rates. For the third quarter, our rate was 4% higher than the industry rate, 86% versus 82%. We were higher during the quarter both in July and August, and then in September, we ended up at 79%, which was the same place the industry ended up, the industry average. I think that drop was impacted by a lot of things. There were a lot of outages across the industry later in the quarter, including some at a couple of Olin locations. I also think that export demand for derivative products was off, it slowed down late in the quarter, and I think that impacted operating rates across the chloro-vinyl sector as well.

Our fourth quarter trend for operating rates, we see as flat to maybe up slightly in our system, as with -- that's a preliminary read for the quarter. We really don't see the industry being much different than what we have seen the trend being late in the third quarter. When we look at the last three years, the fourth quarter, we're looking at is common with what we've seen before. Operating rate decreases in the fourth quarter, earnings decreases based on seasonality, and end-of-year inventory management at our customer locations, but in all those cases, that's put us in a pretty favorable position going into the first quarter of next year.

So, we're not, we're realistic about what we see, but not distressed about what it means in 2014.

Joseph Rupp - *Olin Corp - Chairman, President and CEO*

Yes, just to reaffirm, what our experience has been is that we see the tail-off in the fourth quarter, and we see a bounce-back in the first quarter. And we have no reason not to think that, that would occur next year.

Frank Mitsch - *Wells Fargo Securities, LLC - Analyst*

Okay. Great. And then there was a decline in terms of the inter segment eliminations sequentially. Obviously, this is the first year of KA Steel, or, you know, first full Q3 of KA Steel, we don't have the year-over-year progression. Is that something that's common, or was there something in particular that impacted that decline from Q2 to Q3?

John Fischer - *Olin Corp - SVP and CFO*

I don't think, Frank, you can read anything into that. It goes into the timing of caustic receipts by the Chemical Distribution business and where they come from.

Frank Mitsch - *Wells Fargo Securities, LLC - Analyst*

All right, great. And then John Fischer, you mentioned, I think you said that the cash at the end of the year is going to be similar to the level at the end of Q3, which obviously was at a very high level. Can you speak more broadly in terms of your thoughts on use of cash here, share buyback versus M&A?

John Fischer - *Olin Corp - SVP and CFO*

I think Joe laid out the priorities. He talked about we will continue look at opportunities for accretive acquisitions or investments, share repurchases and then we will look at our dividend policy.

Frank Mitsch - *Wells Fargo Securities, LLC - Analyst*

All right. Thank you so much.



Joseph Rupp - *Olin Corp - Chairman, President and CEO*

Thank you, Frank.

Operator

Sorry, sir. Next we have Andy Cash of SunTrust.

Jason Freuchtel - *SunTrust Robinson Humphrey - Analyst*

Hello, this is Jason Freuchtel in for Andy Cash. Good morning, gentlemen.

Joseph Rupp - *Olin Corp - Chairman, President and CEO*

Good morning.

Jason Freuchtel - *SunTrust Robinson Humphrey - Analyst*

How, if at all, will the sale leaseback transaction impact your transportation costs in the future?

John Fischer - *Olin Corp - SVP and CFO*

You will not see a meaningful change from that.

Jason Freuchtel - *SunTrust Robinson Humphrey - Analyst*

And what's the approximate proportion of leased vs. owned barges and rail cars.

John Fischer - *Olin Corp - SVP and CFO*

At this juncture the vast majority of the all our Chlor Alkali transportation equipment is leased.

Jason Freuchtel - *SunTrust Robinson Humphrey - Analyst*

Okay, great, thanks.

Joseph Rupp - *Olin Corp - Chairman, President and CEO*

Thank you.

Operator

Next we have Christopher Butler with Sidoti & Company.



Christopher Butler - *Sidoti & Company - Analyst*

Hi. Good morning, guys.

Joseph Rupp - *Olin Corp - Chairman, President and CEO*

Good morning.

Christopher Butler - *Sidoti & Company - Analyst*

When we look at the Winchester and your expected savings from the shift down to Mississippi, could you talk to the increase that you indicated this morning? Is this, is there another line that you're moving? Or is this just -- greater than you anticipated

Joseph Rupp - *Olin Corp - Chairman, President and CEO*

It's due to greater -- It's better savings. In reality of it is, we are operating at much higher efficiency levels with that plant.

Christopher Butler - *Sidoti & Company - Analyst*

And with the revenue out of Winchester, could you give us some help on what you think normal is now as -- we have more guns sold, and there's more demand for ammunition, but we're going to be moving off of a peak here at some point in 2014/2015. Where does normal kind of shake out? Can you give us some guidance there?

John Fischer - *Olin Corp - SVP and CFO*

Chris, I think that if you look back at the industry 10 years ago, we would have told you that in a normal year, ammunition demand across the spectrum of all types of ammunition for all types of guns was in the 4 to 5 billion round range. I think that we believe today that that number is probably more like 8 billion per year.

Christopher Butler - *Sidoti & Company - Analyst*

And looking at the distribution business, could you give us a little but more color on your comments about the realignment of provider/distributor relationships in the industry and how that may affect KA Steel and some of its non-Olin customers?

Joseph Rupp - *Olin Corp - Chairman, President and CEO*

I would just suggest that, in the whole industry, everybody is looking at their cost-to-serve models and their value chain. And as a result, there is some rearrangement that's occurring -- throughout the industry.

Christopher Butler - *Sidoti & Company - Analyst*

So it sounds as if this isn't a reaction to Olin now owning KA Steel?

Joseph Rupp - *Olin Corp - Chairman, President and CEO*

We believe it's broader than that.

Christopher Butler - *Sidoti & Company - Analyst*

I appreciate your time. I'll go back in the queue.

Joseph Rupp - *Olin Corp - Chairman, President and CEO*

Thank you.

Operator

Your next question we have comes from the location of Herb Hardt, Monness, Crespi, Hardt.

Herb Hardt - *Monness, Crespi, Hardt & Co. - Analyst*

Good morning.

Joseph Rupp - *Olin Corp - Chairman, President and CEO*

Morning.

Herb Hardt - *Monness, Crespi, Hardt & Co. - Analyst*

Two questions, one is you mentioned that distribution was a bit disappointing. Can you be a little more specific about how you can address that? And secondly, can you talk a little bit about pricing in both bleach and the hydrochloric acid?

John McIntosh - *Olin Corp - SVP, Operations*

The distribution business is disappointing from the perspective that our original plan involved, and one of the premises for the business was, it would have afforded us the opportunity to move Olin-produced products that this distribution company didn't previously sell into their portfolio of products and into the marketplace. That is still our intention, and we're still very, feel very strongly that's an opportunity that we're afforded. But the ramp-up time to make to accomplish that has been longer than we anticipated, so we've had less contribution to the distribution segment earnings from selling those products in 2013 than we had hoped for. We continue to push that initiative so that we will be in better shape with transportation equipment, and storage tanks, and other infrastructure and assets, so that we'll be in a better position to do that in the coming years.

Your second question was about bleach pricing?

Herb Hardt - *Monness, Crespi, Hardt & Co. - Analyst*

Bleach and hydrochloric acid.

John McIntosh - *Olin Corp - SVP, Operations*

Hydrochloric acid pricing is down significantly in any year-over-year comparison because the first quarter of 2012 was, you know, a peak quarter for HCl pricing, and it was just due to availability of product. And we have -- and prices have come down pretty much since then, so we've had a

very unfavorable comparison during that period of time. We expect HCl pricing to move down a little bit, or trend into the fourth quarter. But it's still a very healthy price compared to what it has been historically, and still represents a premium over the sale of chlorine.

On the bleach side, we didn't see a lot of pricing change over the course of the year. We were slightly off of our budgeted forecast for bleach pricing. A lot of that was driven by the fact that, you know, chlorine caustic prices drifted down during part of the year. But we, again, still see our bleach pricing reflect a premium over selling ECUs into the marketplace. And that's what we really watch and what we really focus on achieving.

Herb Hardt - *Monness, Crespi, Hardt & Co. - Analyst*

Thank you.

Operator

Your next question we have comes from Don Carson with Susquehanna.

Bobby Geornas - *Susquehanna Financial Group - Analyst*

Hi, this is Bobby Geornas for Don Carson. You referenced an expectation for an uptick in the beginning of the year in terms of ECU value, but I guess the difference this time around is the capacity additions that are coming online. Are you factoring in or assuming some sort of capacity shutdowns for 2014 in that assessment? And the second part of the question is, short of Winchester becomes sort of a bigger part of the overall earnings profile in 2014, has that changed how you think about the -- your dividend policy?

Joseph Rupp - *Olin Corp - Chairman, President and CEO*

If you take us back to the beginning of the year, I think our forecasts were actually, we thought that there would be a higher level of demand in addition to the fact that we were skeptical as to when the new capacity was going to come on line. The reality of it is that there is no increase in demand in North America for both chlorine and caustic this year.

Our view is that the most important element here is chlorine demand will drive operating rate irrespective of new capacity. So as we go forward next year, we would have to see some increases in demand. If there are no increases in demand for chlorine, we're going to get a tight caustic market, which is really what, where our thinking is at this point in time. From a Winchester perspective, your question on Winchester was?

John Fischer - *Olin Corp - SVP and CFO*

As it related to the dividend.

Joseph Rupp - *Olin Corp - Chairman, President and CEO*

I think what John and I both have said is that we're going to continue to take a look at three different things, which is first and foremost, accretive acquisitions, second is share repurchases, and third is our dividend policy. All three are co-equal in our view.

Bobby Geornas - *Susquehanna Financial Group - Analyst*

Okay, thank you.



Operator

The next question we have comes from the location of Edlain Rodriguez of UBS.

Edlain Rodriguez - UBS - Analyst

Thank you Good morning, guys. Just follow up on the distribution business. I mean, yes, you did say it's a disappointment. I mean can you talk about like how long you expect it to get to where you want it to be? I mean right now, it's not there yet. I mean are we talking about a couple of quarters, or is it a year before it gets to where you think it should be?

Joseph Rupp - Olin Corp - Chairman, President and CEO

We feel it's going to take us one to two years to get it where we want it.

John Fischer - Olin Corp - SVP and CFO

But we always said it would take us three years for the, to realize the full value of the synergy. So we're a little slower out of the gate, and we should get there at the end at the same time.

Joseph Rupp - Olin Corp - Chairman, President and CEO

That's fair.

Edlain Rodriguez - UBS - Analyst

Okay. Understand. And on the chlorine demand, as you say you're not seeing the demand right now. What's driving that lack of demand and how is that going to change in 2014?

John McIntosh - Olin Corp - SVP, Operations

When we look at the various sectors that we serve, there were a lot of -- most all of the sectors, demand sectors maybe with the exception of vinyls were either flat or only slightly changed when we look at third quarter versus historical third quarter or even the first three quarters of 2013 compared to 2012. I mentioned that the exception is the vinyl sector. When you look at chlorine derivatives being exported from this country, that number is up significantly, 20% comparing July year-to-date 2013 versus July year-to-date 2012. So that sector is growing because of energy costs.

We are the most competitive place in the world to produce that, produce those commodities and export it. But we've not seen any broad-based, you know, increase in historical demand for any of the chlorine sectors that we serve. And we really are involved in every one of them in the North American sector, North American demand sectors.

Edlain Rodriguez - UBS - Analyst

Thank you.

Operator

Next is the location of Eugene Fedotoff of Longbow Research.

Eugene Fedotoff - *Longbow Research - Analyst*

Good morning, guys. Thank you for taking my question. First, I guess on your EBITDA guidance, full year guidance was updated. What was the major difference between the guidance that you provided in the third quarter, in the second quarter, I'm sorry, and the updated guidance? What was the biggest surprise?

John Fischer - *Olin Corp - SVP and CFO*

The weakness in chlorine demand, and the decline -- forecasted decline in caustic pricing.

Eugene Fedotoff - *Longbow Research - Analyst*

Okay, got it. I thought you talked on the last conference call about \$30 per ton of caustic prices realized in the index, and you expect that the in your numbers in third quarter, was that the case? Was it fully offset by lower chlorine prices or was it not realized?

John McIntosh - *Olin Corp - SVP, Operations*

There was \$30 caustic price increase that was announced the end of August. And when we were reviewing, and there were price increases earlier in the year as well on caustic. When we were talking about our forecast for the third quarter, we expected some of the price increases announced in the second quarter to, in fact, take hold, and none of those price increases occurred. And as a matter of fact, as we've said in our comments, there have actually been price decreases reflected in some of the indexes. So our expectation of price, caustic price moving upward just was not realized during the quarter because the overall industry didn't support the price increase that was announced.

Eugene Fedotoff - *Longbow Research - Analyst*

Do you expect the shortages in caustic in the fourth quarter as you mentioned, that there is going to be some price announcements?

John McIntosh - *Olin Corp - SVP, Operations*

Well, I can speak for Olin's system. The operating rate numbers that we saw in September, 79%, a drop of over 10% in our system, and a significant drop in the industry numbers as well. If those continue, I believe we will see caustic get tight.

We already have put caustic on order control, in Olin's system because we expect if this trend on operating rates continues, we will have trouble supplying caustic to all of our customers in the fourth quarter. And again, if that follows in the industry, then I would not be at all surprised to see caustic price increase activity announced in the fourth quarter for implementation in the first half of 2014.

Eugene Fedotoff - *Longbow Research - Analyst*

Great. Just the last question on Winchester. Did you see any impact from government shutdowns on orders in the quarter?

John Fischer - *Olin Corp - SVP and CFO*

No, we have not.



Eugene Fedotoff - *Longbow Research - Analyst*

Great, thank you very much.

Operator

Next we have the location of Edward Yang, Oppenheimer.

Edward Yang - *Oppenheimer & Co. - Analyst*

Hi, good morning, guys. Quick question, I might have missed this. What was the Winchester commercial backlog this quarter, and what was it the last two quarters?

John Fischer - *Olin Corp - SVP and CFO*

It was \$439 million at the end of this quarter. It was just shy of \$500 million at the end of the second quarter, and at the end of the first quarter, it was more in the \$400 million range.

Edward Yang - *Oppenheimer & Co. - Analyst*

So the backlog declined sequentially somewhat? What was the reason for that?

John Fischer - *Olin Corp - SVP and CFO*

That's just the seasonal sales.

Joseph Rupp - *Olin Corp - Chairman, President and CEO*

The nature.

Joseph Rupp - *Olin Corp - Chairman, President and CEO*

Yes.

Edward Yang - *Oppenheimer & Co. - Analyst*

And what's the D&A in Winchester?

John Fischer - *Olin Corp - SVP and CFO*

About \$15 million a year.



Edward Yang - *Oppenheimer & Co. - Analyst*

Okay, great. And Joe, you mentioned long-term Winchester EBITDA, \$100 million to \$110 million. I think that's up from your prior expectation of \$85 to \$100 million. So that assumes, again, I guess the long term number was 2016 with synergies and savings from the relocation of \$30 million. So this up sizing, if I recall correctly your answer to another question, that was coming from up sizing that \$30 million synergy to \$40 to \$45 million?

Joseph Rupp - *Olin Corp - Chairman, President and CEO*

No. No. We're uping that synergy in the \$35 million range is really where it is. \$35 to \$40 million is what we're saying. So we're up sizing that, but I think there's also more confidence in the fact there's, that the demand level is going to be higher on a normalized basis than where it was prior.

Edward Yang - *Oppenheimer & Co. - Analyst*

Okay. And in terms of how quickly are you also truncating how quickly you get to that long-term number again the previous number was --?

Joseph Rupp - *Olin Corp - Chairman, President and CEO*

No, end of 2015 is where we are. Yes.

Edward Yang - *Oppenheimer & Co. - Analyst*

Okay, so still at the end of 2015.

Joseph Rupp - *Olin Corp - Chairman, President and CEO*

Yes.

Edward Yang - *Oppenheimer & Co. - Analyst*

Moving on to the Chlor Alkali side of the business, just a question on ECU netbacks. Again, you mentioned caustic, You expect to decline \$50 a ton in the 4Q. What's your expectation on chlorine pricing?

John McIntosh - *Olin Corp - SVP, Operations*

I think the number we used in the fourth quarter was \$20 reduction in the ECU, which is predominantly caustic. Chlorine prices are right now are tending to move sideways.

Edward Yang - *Oppenheimer & Co. - Analyst*

Okay. But if you're hopeful that chlorine operating rates, low chlorine operating rates are going to support caustic prices, is that going to cause some weakness in the chlorine price? Or do you think it will just continue moving sideways?

John McIntosh - *Olin Corp - SVP, Operations*

We don't expect there to be any significant weakness which is going to cause a significant change in chlorine pricing.



Edward Yang - *Oppenheimer & Co. - Analyst*

Okay, and just a final question on the Chlor Alkali side of the business. Again, a lot of focus and attention being paid to ECU netbacks which I understand, but maybe a question for John. ECU netbacks in 2011 was \$568 for Olin. This year, you'll probably end around somewhere like \$570, so it's been kind of flat sideways for the last two years.

But the Chlor Alkali margins have come under some pressure. Your Chlor Alkali earnings in 2011 were \$235 million, operating income. This year, you probably would be down below \$200 million. So, with flat pricing and operating rates up slightly, why have the Chlor Alkali earnings been sideways to down?

John McIntosh - *Olin Corp - SVP, Operations*

Well I think we've been investing in and starting up new facilities to satisfy our strategic intent to consume more of our ECUs, and hydrochloric acid and into bleach. I think we have continued to see although in our remarks we did note that the percentage was smaller than historical, increases in freight rates, which has been a drag on earnings as well.

John Fischer - *Olin Corp - SVP and CFO*

I think, Edward, if you look back and did a comparison of segment EBITDA 2011 to 2013, the magnitude of the change is not nearly as great. The amount of depreciation expense running through Chlor Alkali has grown by about \$30 million, because of the Charleston conversion, and then the investments John talked about in HyPure bleach and HCl.

There has been some higher electricity costs in 2013 than there were in 2011 just because of where natural gas has been. And we've had turn around costs in 2013 that we didn't have in 2012 or 2011. But I think if you looked at it on an EBITDA basis, you'll find it's much closer to flat.

Edward Yang - *Oppenheimer & Co. - Analyst*

So, if you read you right, John Fischer, then the -- your expectation going forward is if ECU netbacks were to increase, that would be margin accretive to your Chlor Alkali business?

John Fischer - *Olin Corp - SVP and CFO*

Yes, they would.

Edward Yang - *Oppenheimer & Co. - Analyst*

All right. Thank you for your time.

Operator

Next we have Richard O'Reilly of Revere and Associates.



Richard O'Reilly - *Revere and Associates - Analyst*

Good morning. Thank you, gentleman. Two quick questions. The first, you kind of touched on this before, but your volume, your chlorine caustic volumes were down a couple percentage points year over year. And last year third quarter, you were down a few points, year-over-year. So my question is how much do you think that combined decline is economic versus your strategy of shifting the molecule to bleach and to HCl?

John McIntosh - *Olin Corp - SVP, Operations*

It's economic.

Richard O'Reilly - *Revere and Associates - Analyst*

So you haven't had, you haven't shifted in the last couple of years of the molecules to bleach? Am I missing something?

John McIntosh - *Olin Corp - SVP, Operations*

No, we have shifted and that has increased the amount of chlorine we put into those products, but that is not a negative impact on operating rates. Those ECUs produced and later converted still count as part of our operating rate.

Richard O'Reilly - *Revere and Associates - Analyst*

Okay. But the absolute volume of chlorine caustic has declined, and that's --?

John Fischer - *Olin Corp - SVP and CFO*

The amount of product we have sold as chlorine has declined. That's because of economic reasons. We've been able to offset some of that by selling more as HCl, and more as bleach.

Richard O'Reilly - *Revere and Associates - Analyst*

Fine. Second question is did you -- I know in July you had talked about the contract settlement, but did you ever discuss how it came about?

Joseph Rupp - *Olin Corp - Chairman, President and CEO*

We did not. We just said it was and we were not at liberty to talk how it came about.

John Fischer - *Olin Corp - SVP and CFO*

But it was in our third quarter guidance.

Richard O'Reilly - *Revere and Associates - Analyst*

Right. Yes. Okay, good. Thanks a lot.

Joseph Rupp - *Olin Corp - Chairman, President and CEO*

Thank you.

Operator

Well, this concludes our question and answer session. I would now like to turn the conference back over to Mr. Joseph Rupp for any closing remarks. Sir?

Joseph Rupp - *Olin Corp - Chairman, President and CEO*

We would like to thank you for joining us this morning. And look forward to sharing our full year results with you in January. Thank you.

Operator

And we thank you, sir, and to the rest of management for your time today. The conference call is now concluded. At this time, you may all disconnect your lines. Thank you for attending today's presentation. Take care and have a great day.

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